Circuit Court, Eastern District of Arkansas.

CREDIT COMPANY (LIMITED) OF LONDON, ENGLAND, *v.* ARKANSAS CENT. RAILROAD CO., AND OTHERS.

A court of equity may authorize the receiver of a railroad to issue certificates of indebtedness and make them a first lien upon the road, for the purpose of raising funds to make necessary repairs and improvements, but it is a power to be sparingly exercised; and when the road cannot be kept running without its exercise, except to a very limited extent, the sound policy is to discharge the receiver, or stop running the road and speed the foreclosure.

In the absence of fraud the beneficiaries in railway mortgages are bound by what is done by their trustees.

Where a holder of railroad bonds alleged the trustee had filed a bill and obtained a decree of foreclosure for the principal of the bonds not due, as well as for the interest which was due, without the written request of the holders of one-third in amount of the bonds, which it was claimed was a necessary prerequisite by the terms of the mortgage to the exercise of the power to declare the principal debt due, and sought for this reason to avoid the foreclosure proceedings, *held*, (1) that it was competent for the trustee to file a bill to foreclose for the interest due: (2) that the plaintiff ratified the action of its trustee by filing and proving in the master's office, in the foreclosure proceedings, more than one-third in amount of all the bonds issued; and (3) that the absence of such a requisition did not affect the jurisdiction of the court, and a decree for a larger sum than was due was error merely, to be corrected on appeal; and that as the error was one of which the trustees could not complain, and there was no fraud, the bondholders were as much bound as the trustee, and could not avoid the decree, on this ground, in any form of proceeding.

When the property of a railroad company is sold under a decree of foreclosure, at which all persons are authorized to bid, the fact that it is purchased by the president of the company in his individual right will not in itself raise a trust relation between him and a holder of the bonds of the company, which will entitle the latter to treat him as a trustee of the property so purchased.

One claiming the right to avoid a purchase made by another at a judicial sale, or of treating the purchaser as a trustee, and availing himself of the purchaser's bid, cannot delay the assertion of this right to enable him to decide in the light of subsequent events whether he would or not be profited by its assertion.

IN Equity.

N. & J. Erb, for plaintiffs.

U. M. and *G. B. Rose*, and *C. C. Waters*, for defendants.

The opinion of the court was delivered by

CALDWELL, J.—The Arkansas Central Railroad Company was formed for the purpose of constructing a railroad from Helena to Little Rock, with a branch to Pine Bluff. The chief ultimate promoters of this enterprise were Stephen W. Dorsey and J. E.

Gregg. Dorsey was the president of the company, and its financial agent and manager, and generally controlled and conducted all the affairs of the corporation.

What is commonly called an exhaustive contract was entered into between the company and J. E. Gregg & Co. for the construction of the road, by the terms of which Gregg & Co. were to build the road for all its stock subscriptions and other assets, and a majority of its stock.

The directors of the railroad company and all its officers, except the president, seem never to have had more than a mere nominal existence after the making of this contract, From that time Gregg & Co. were regarded as owners of the road, and its assets in hand, as well as all that might thereafter be acquired.

Dorsey was a member of this firm also, and in the double capacity of president of the railroad company, and a member of the firm of Gregg & Co., he seems to have managed the financial affairs of both.

The company executed a mortgage to secure its first mortgage bonds, which were put upon the market and sold to the amount of $720,000. The defendant, the Union Trust Company of New York, was the trustee in this mortgage. Dorsey went abroad to effect a sale of the bonds, and succeeded in placing most of them in London and Amsterdam.

By the fall of 1872, forty-eight miles of the road, which was a narrow gauge, had been completed in an imperfect manner. The work of construction was never resumed after that date. About this time Dorsey engaged actively in politics, and having been elected to the United States senate in the early part of 1873, and the assets and resources of the railroad company having been exhausted, he and the firm of J. E. Gregg & Co. soon ceased to take any further interest in the enterprise; and the defendant Johnson, who had at the solicitation of Dorsey invested some money in the concern of J. E. Gregg & Co., was elected president, and had the control and management of the road, and the affairs of the company from that time until the commencement of proceedings to foreclose. The company had neither resources nor credit, and the earnings of the road were barely sufficient to keep it running, without making needed repairs and improvements. The construction of the forty-eight miles of road seems to have absorbed the proceeds of the $720,000 first-mortgage bonds of the company, and of state

aid and state levee bonds, and county and municipal subscriptions, amounting in the aggregate to some $2,000,000. The company was hopelessly insolvent. No interest was paid on its first-mortgage bonds, and on the 20th day of September 1876, the trustee filed a bill in the United States District Court at Helena, then in the western district, to foreclose the mortgage. The bill alleged that the holders of one-third in amount of the bonds had requested the trustee to foreclose. A receiver was appointed, upon whose application Judge PARKER authorized the issue of receiver's certificates to the amount of $75,000, to make necessary repairs and improvements on the road. Between the date of this order and the next term of the court, Helena was transferred to this district, and the judge of this district rescinded the order authorizing the receiver to issue certificates. The rescinding order was not made because the road did not stand in need of repairs. It was notoriously true that its condition was such as to make it dangerous to life and property to run cars over it; ties were rotten, iron worn out, rolling stock in bad condition, bridges insecure, culverts washed out, and the road-bed in many places too low, resulting in over-flows of the track and stoppage of trains. No repairs nor betterments had been put upon the road since it had been built.

It seems to be settled that a court of equity has the power in this class of cases to authorize its receiver to issue certificates of indebtedness, and make them a first lien upon the road, for the purpose of raising funds to make necessary repairs and improvements: *Wallace* v. *Loomis*, 97 U. S. 146, 162; s. c. 2 Woods 506, under title, *Stanton* v. *Alabama & C. Railroad Co.*

But it is a power to be sparingly exercised. It is liable to great abuse, and while it is usually resorted to under the pretext that it will enhance the security of the bondholders, it not unfrequently results in taking from them the security they already have, and appropriating it to pay debts contracted by the court. The history of *Wallace* v. *Loomis*, *supra*, furnishes an instructive lesson on this subject.

This court has uniformly refused to arm its receivers with such a dangerous power. When the road cannot be kept running without its exercise, except to a very limited extent, the safe and sound practice is to discharge the receiver or stop running the road, and speed the foreclosure.

In the case of *Paine* v. *Little Rock & Ft. S. Railroad Co.*,

April term, 1874, application was made to this court to authorize a receiver to issue certificates, which were to be a first lien, to build sixty miles of road, in order to earn a large and valuable land grant, which would lapse in a short time unless the road was completed. A majority in value of the first-mortgage bondholders, concurred in the application: and the orders of the court in the case of *Stanton* v. *Alabama & C. Railroad Co.*, 2 Woods 506 (the case was not then reported), and the case of *Kennedy* v. *St. Paul & Pac. Railroad Co.*, 2 Dill. 448, were pressed upon the attention of the court. But the order was refused upon the ground that it was no part of the duty of a court of chancery to build railroads, and that the assent of all the parties interested in the property could not make it such. And there is no difference, so far as relates to this question, between building a railroad and making extensive and general repairs and betterments, the cost of which sometimes approximates the cost of original construction. In the case referred to, of the Fort Smith railroad, the proceedings to foreclose were speeded, and a decree rendered to meet the exigencies of the case, which the Supreme Court approved, and said "was a much more desirable plan" than to issue receiver's certificates: *Shaw* v. *Railroad Co.*, 100 U. S. 612.

Before the order authorizing the receiver to incur debts for repairs and other purposes was rescinded, he had incurred debts to the amount of some $22,000, chiefly for ties and a machine-shop. The ties were indispensable if trains were to be kept running, and the machine-shop was a necessary and valuable property to the road, and its use a necessity, though that could probably have been had without purchasing the property. A final decree of foreclosure was rendered on the 17th day of March 1877. By the terms of the decree the purchaser was required to pay $40,000 in cash. This sum was required to pay the receiver's certificates, and other costs and expenses of foreclosure. Any amount bid in excess of the $40,000 could be paid in first-mortgage bonds. Unusual pains were taken to convey to the bondholders actual notice of the foreclosure proceedings, and holders of $661,000, out of a total of $720,000 of the first-mortgage bonds had actual notice of the foreclosure proceedings, and the time and place of sale. The present plaintiffs had opened negotiations looking to a foreclosure of the mortgage before the bill for that purpose was filed by the trustee; and before the sale under the decree it filed and proved in the

master's office bonds to the amount of $461,000, being the very bonds on which this suit is bottomed. The road was sold at the master's sale for $40,000 to S. H. Horner, as trustee for A. H. Johnson, the then president of the railroad company, and superintendent of the road under the receiver.

The plaintiff, by its agent, had notice of this sale, and appeared, by its attorney, in court and moved to open the biddings for the road, and the court passed an order that the biddings would be opened if the present plaintiff or any person should advance the bid $5000 during a period of ten days allowed for that purpose. The plaintiff, or its agent, declined to open the biddings. In the meantime Johnson had grown sick of his bargain, and made application to the court to set aside the sale and permit him to withdraw the purchase-money. This was refused, and the sale confirmed. Johnson then offered to turn the road over to the plaintiff, or any holders of the first-mortgage bonds who would pay him the amount of his bid within a period of some fifty days. This offer was communicated to the plaintiff by its agent, Sully, and declined.

It is clear, from the evidence, that the defendants Johnson and Horner and the citizens of Helena wished to have the bondholders purchase the road. They were extremely anxious that the road should be completed, and believed that its purchase by the bondholders would insure that result, and that nothing else would. After the plaintiff and other bondholders declined to take Johnson's purchase off his hands, he proceeded, as fast as he could raise means for that purpose, to put the necessary repairs and improvements upon the road, which embraced 50,000 new ties, five miles of new iron, the rebuilding of nearly all the bridges and culverts, raising the road-bed in many places, and expensive repairs of the rolling stock. He afterwards sold a half interest in the property to his co-defendant, John J. Horner. Not long after the purchase, railroad securities and property in the south appreciated very much, and, although the road in question was but a fragment, its value was enhanced by the general and unprecedented increase in the value of all railroad property. Its value was further enhanced by the construction of a trunk line—not projected when Johnson purchased—from Missouri to Texas, which connects with its western terminus at Clarendon, and by the extensive repairs and improvements put upon the road, which altogether made it worth from $100,000 to $200,000 at the time this suit was commenced, sup-

posing it to be free from incumbrances prior in time to the mortgage under which defendants claim.

The bill, which was filed five years after the sale, seeks to charge Johnson as a trustee for the bondholders on general charges of fraud against him, the Union Trust Company, and others, relating to the foreclosure and sale, and for alleged inadequacy of price. The latter charge was abandoned at the hearing, the counsel for the plaintiff conceding on the argument that the road sold for all it was worth in its then condition, and in view of the question of the lien for the state aid bonds.

The rule is well settled that in the absence of fraud the beneficiaries in railway mortgages are bound by what is done by their trustee.

"In such cases the trustee is in court for and on behalf of the beneficiaries; and they, though not parties, are bound by the judgment, unless it is impeached for fraud or collusion between him and the adverse party. The principle which underlies this rule has always been applied in proceedings relating to railway mortgages where a trustee holds the security for the benefit of the bondholders:" *Kerrison* v. *Stewart*, 93 U. S. 155, 160. "The trustee of a railroad mortgage represents the bondholders in all legal proceedings carried on by him affecting his trust, to which they are not actual parties, and whatever binds him, if he acts in good faith, binds them. If a bondholder not a party to the suit can under any circumstances bring a bill of review, he can only have such relief as the trustee would be entitled to in the same form of proceeding:" *Shaw* v. *Railroad Co.*, 100 U. S. 605, 611. Although the bill charges fraud in general terms upon the trustee, in connection with the foreclosure suit, there is not a syllable of evidence to support the charge.

One point much relied on at the hearing to support the bill was that the bill to foreclose was filed by the trustee without the written request of the holders of one-third in amount of the bonds then outstanding, as required by the twelfth article of the mortgage; and that the decree requiring the payment of the principal sum of the mortgage debt was therefore erroneous. The late cases of the *Chicago, D. & V. Railroad Co.* v. *Fosdick*, 106 U. S. 47, are cited in support of this contention. The ruling in those cases does not aid the plaintiff's case, for several reasons: 1. The mortgage in the case at bar contains an important provision on

the subject which was not contained in the mortgage under consideration in the cases cited, and which would seem to authorize all that was done by the trustee, and the decree of the court for the whole debt. 2. It was undoubtedly competent for the trustee to file a bill to foreclose for the interest actually due, and that largely exceeded in amount the value of the road. 3. The railroad company does not complain of the decree, and the plaintiff is estopped to do so by reason of having filed and proved in the master's office more than one-third in amount of all the bonds issued, with full knowledge of all the facts. This was a ratification of the action of the trustee. 4. If it be conceded that the requisition of the holders of one-third in amount of the bonds was indispensable to authorize a decree for the full sum of the mortgage debt, that fact would not affect the jurisdiction of the court or the validity of its decree when collaterally attacked. The jurisdiction of the court to pronounce a decree in the case is not contested, and if it rendered a decree for more than was due it was error merely, which might have been corrected on appeal by the proper party in apt time. But if it be conceded that it was an error, it was one of which the trustee could not complain; and there being no fraud on the part of the trustee the bondholders are as much bound as the trustee, and cannot avoid the decree in any form of proceeding: *Shaw* v. *Railroad Co.*, *supra.*

It is needless to discuss in detail the charges of fraud contained in the bill. The plaintiff has lost all right to be heard by its own gross laches. In excuse for the long delay, the bill alleges the plaintiff was ignorant of the facts until recently. This allegation is not true. The plaintiff's agent had notice of all the facts, and testifies he communicated them to the plaintiff immediately after the sale. But the bill itself does not state a case that will excuse the delay. "A general allegation of ignorance at one time and knowledge at another is of no effect. If the plaintiff made any particular discovery it should be stated when it was made, what it was, how it was made, and why it was not made sooner. * * * There must be reasonable diligence, and the means of knowledge are the same, then, in effect as knowledge itself:" *Wood* v. *Carpenter*, 101 U. S. 135, 140; *Harwood* v. *Railroad Co.*, 17 Wall. 78; *Badger* v. *Badger*, 2 Id. 87.

In *Harwood* v. *Railroad Co.*, *supra*, there was a delay of five

years, and in *Twin-lick Oil Co.* v. *Marbury*, 91 U. S. 587, there was a delay of four years, and the court denied relief in both cases on the ground of laches. In the case last cited, the defendant, at the time he purchased the corporate property, was a stockholder and director in the company, and the bill, which sought to charge him as a trustee, was filed by the company, and not, as in the case at bar, by a bondholder. All parties in this case were authorized to bid at the sale, and the fact that Johnson was president of the railroad company and the plaintiff a holder of bonds of the company did not in itself raise a trust relation between them which would entitle the latter to charge the former as a trustee, and at his election treat his purchase as though made in trust for its benefit. It could only avail itself of Johnson's purchase by virtue of some agreement or fraudulent act on his part. The plaintiff does not rely upon any agreement, and if the conduct of Johnson was such as to entitle the plaintiff to avoid his purchase or avail itself of his bid, it ought to have exercised the right within a reasonable period. It could not delay the assertion of this right to enable it to decide, in the light of subsequent events, whether it would or not be profited by its assertion.

In *Twin-lick Oil Co.* v. *Marbury*, *supra*, Mr. Justice MILLER says: "No delay for the purpose of enabling the defrauded party to speculate upon the chances which the future may give him of deciding profitably to himself whether he will abide by his bargain or rescind it, is allowed in a court of equity." That is precisely what the plaintiff asks the court to permit it to do in this case. It declined to take the property at the price bid by Johnson, because as matters then appeared, that seemed to be all or more than the property was worth. It was patent to all at the time of the sale that the alternative would be presented to the purchaser of expending at once a large sum for repairs and improvements on the road, or abandoning its use as a railroad altogether. And after these expenditures had been made it was exceedingly doubtful whether the earnings of the road would equal its running expenses. In view of these facts, and the further fact that it was claimed then that the lien for the $1,350,000 state aid bonds issued to the road was paramount to the lien of the mortgage under which the road was sold (which is still an open question so far as relates to this road), it is not surprising that it was difficult to find a bidder for the property at the minimum price fixed in the decree, or that

the plaintiff declined to take it at that price. Years afterwards, and when the property had greatly increased in value from causes not then foreseen, and from extensive repairs and improvements put upon it, and after other interests had intervened, and the plaintiff erroneously supposed the question of the lien for the amount of the state aid bonds was out of the way, it files this bill, and asks that it be permitted to do now what it declined to do then, take the property at Johnson's bid, and that he be decreed to be a trustee and required to account.

A more inequitable demand, considering the facts of the case, was probably never addressed to a court of equity. If it was settled that there was no lien on the road to secure the state aid bonds, the case would not be any more favorable for the plaintiff. Having declined to take the risk of purchasing the property when it was doubtful whether the investment would entail a loss or yield a profit it should not be permitted at this late day and in the light of subsequent events to reconsider that resolution. The profits, if in the end there are any, justly belong to the purchaser, who took the risk, and whose labor and capital have added largely to the value of the property. As was said by the court in *Wood* v. *Carpenter*, *supra*, it is impossible "to avoid the conviction that the plaintiff's conduct marks the difference between forethought in one condition of things and afterthought in another."

Laches need not be pleaded. If the objection is apparent on the bill itself, it may be taken by demurrer: *Maxwell* v. *Kennedy*, 8 How. 222; *Lansdale* v. *Smith*, 16 Cent. Law J. 28; s. c. 1 Sup. Ct. Rep. 350. And if the cause, as it appears on the hearing, is liable to the objection, the court will refuse relief, without inquiring whether there is a demurrer, plea or answer setting it up: *Sullivan* v. *Portland Railroad Co.*, 94 U. S. 811; *Badger* v. *Badger*, 2 Wall. 95.

The plaintiff and all other purchasers of the first-mortgage bonds have undoubtedly lost the money invested in them. But they did not lose it by the foreclosure proceedings. It was lost from the instant it was invested in bonds secured by a mortgage on a road which had an existence only in name. If they have any just ground of complaint, it would seem to be against those whose representations induced them to purchase the bonds, and who probably used the proceeds for purposes other than building the road.

Let a decree be entered dismissing the bill for want of equity, at plaintiff's costs.

AUTHORITY TO ISSUE RECEIVERS CERTIFICATES.—A mortgagee taking possession of the property mortgaged may expend upon it such sums as are necessary to preserve it from waste and dilapidation which might otherwise depreciate the security in value, or even render it entirely worthless. So a receiver taking possession on behalf of the mortgagee may expend money to stay waste or destruction of the security of his mortgagee. He may do whatever the mortgagee might himself do to preserve the property.

This is true of receivers of railways. They may use so much as may be necessary of the revenues of the road, during their possession of it, for the purpose of operating it and keeping it in good repair, suitable for the safe and rapid conveyance of persons and property. A stronger reason exists in the case of receivers of railways for allowing them thus to expend the revenues of the road, or even to borrow money to keep it in good running order and repair, than in the cases of receivers in possession of property purely private, such as a farm or a factory. This reason is the protection of the public in the continued use of the railway as a public highway. "If it were not for the public quality belonging to them, for the injury that would be done to the interests of whole communities that have become dependent on a railroad for accommodation in a thousand things, a chancellor might say to the parties most interested: 'Unless you furnish means for the protection of this property, which does not itself afford an adequate income for this purpose, it may become a dilapidated and useless wreck.' But the inconvenience and loss which this would inflict on the population of large districts, coupled with the benefit to parties who perhaps are powerless to take care of themselves, of preventing the rapid diminution of value and derangement and disorganization which would otherwise result, seem to require —not for the completion of an unfinished work, or the improvement, beyond what is necessary for its preservation, of an existing one, but to keep it up, to conserve it as a railroad property, if the court has been obliged to take possession of it—that the court should borrow money for that purpose, if it can not otherwise do so in sufficiently large sums, by causing negotiable certificates of indebtedness to be issued constituting a lien on the proceeds of the property, and redeemable when it is sold or disposed of by the court." Per MANNING, J., *Meyer* v. *Johnston*, 53 Ala. 348. And to the effect that a receiver may borrow money to preserve in good repair and condition the railway property intrusted to him, see *Hoover* v. *M. & G. L. Railroad Co.*, 29 N. J. Eq. 5; *Meyer* v. *Johnston*, 53 Ala. 237; *Kennedy* v. *St. P. & P. Railroad Co.*, 2 Dill. 448; *Jerome* v. *McCarter*, 94 U. S. 734; *Bank of Montreal* v. *C. C. & W. Railroad Co.*, 7 Cent. L. J. 267; 48 Iowa 518; *Stanton* v. *A. & C. Railroad Co.*, 2 Woods 506; *Wallace* v. *Loomis*, 97 U. S. 146; *Cowdrey* v. *Railroad Co.*, 1 Woods 331; *V. & C. Railroad Co.* v. *V. C. Railroad Co.*, 50 Vt. 14; Am. Ry. Rep. 497.

But may a court authorize a receiver to borrow money to buy new rolling stock, or new shops, to complete an unfinished road, or, still further, to build a new road as an extension, branch or feeder of the railway in his possession? Several cases answer this question affirmatively. In *Gibert* v. *Washington City, &c., Railroad Co.*, 33 Grat. 586, the court, without deciding the question as to the power of the court as an original proposition to make such expenditure, affirmed an order authorizing the disbursement of $10,000 for the construc-

tion of a branch road by the receiver, he having in fact already constructed it for about $8000, it proving a profitable feeder to the main line, and no objection to the expenditure having been made for more than two years. In *Meyer* v. *Johnston*, 53 Ala. 339, 341, the court refer to manuscript opinions in the cases of *Southerland, Trustee*, v. *Lake Superior Ship Canal Railroad & I. Co.*, before U. S. district Judge LONGYEAR, at Detroit, and *Hyde* v. *Soders Point Railroad Co.*, wherein receivers were authorized to borrow money to complete unfinished work. The former case came before the U. S. Supreme Court *sub nom. Jerome* v. *McCarter*, 94 U. S. 738, and the receiver's action in raising money to complete the work—a canal—by the issuance and sale of certificates of indebtedness, secured by his mortgage, was justified. "The canal was unfinished," say the court, "and there were in the receiver's hands no funds to finish it. Hence there was a necessity for making the order which the court made—a necessity attending the administration of the trust the court had undertaken. The order was necessary alike for the lien creditors and for the mortgagors." See also *Wallace* v. *Loomis*, 97 U. S. 162; *Stanton* v. *Ala. & Chat. R. R. Co.*, 2 Woods 506; *Wallace* v. *Loomis*, 97 U. S. 146.

In *Kennedy* v. *St. P. & P. Railroad Co.*, 2 Dill. 448, to prevent a valuable land grant in favor of a railroad company from lapsing, a receiver was appointed *at the instance of bondholders* of the company, whose principal security was said lands, and at their desire he was empowered to borrow money to complete the unfinished portions of the road, and his certificates were made a first lien on the road and lands of the company.

In *Miltenberger* v. *Railway Company*, 106, United States 206, authority was given the receiver to purchase new rolling stock, complete five miles of railway, build a bridge, and pay indebtedness to connecting roads for freight and ticket balances incurred before the receiver was appointed. By the construction of the five miles of railway and the bridge the company secured large donations in land and money, besides adding greatly to its business, and was enabled to transact properly the business it already had. Any indebtedness created by the receiver for these purposes was made a "first lien prior to all incumbrances upon said road." The order was affirmed by the Supreme Court of the United States.

From these cases the power to authorize a receiver in a proper case to issue and sell certificates to purchase new equipment, or to build new roads, would seem to be pretty firmly established, at least in extraordinary cases where such action by the receiver is deemed necessary for the security of the mortgagees.

But in *Meyer* v. *Johnston*, 53 Ala. 340, it was pointed out that, in preceding cases, the issue and the sale of receiver's certificates had been consented to by the prior mortgagees; and it was decided that a railroad receiver could not, in order to raise money to complete the road, create liens upon its property which will displace older liens. It was sought to compare such certificates to a bottomry bond, whose lien takes precedence of all prior claims on the vessel. The court refused to take this view. "A ship far from home, in distress and without resource, must perish, and perhaps her crew with her, if a bottomry bond, given then for repairs and supplies shall not have precedence of other liens upon the vessel. But the court does not consider a railroad on *terra firma* so beyond the reach of help from those who own it or are concerned in it, as to justify the adoption in such a case, of the rule relating to a ship abroad and about to perish." *Meyer* v. *Johnston*, 53 Ala. 345.

It was further pointed out that the railway company could not itself issue such obligations and give them the first

lien upon its property as against prior mortgagees or other lien holders. Its contracts were inviolable and it would not be permitted to impair them. Further, referring to the provision in the United States Constitution prohibiting a state from impairing contracts, the court said: "And certainly a court which is a portion of the government of a state cannot have power which is denied to the state in convention assembled. If, therefore, the action of a chancellor in this cause goes to the extent of taking the property of the defendant corporation into his hands for the purpose, through his appointees, of completing an unfinished work, or of enlarging or improving a finished one, beyond what is necessary for its preservation, and to that end—of raising money by charging the railroad and its appurtenances with liens which are to supersede older ones without the consent of the holders of these, he has inadvertently passed beyond the boundaries of a chancellor's jurisdiction. In our opinion no such power is vested or resides in any judicial tribunal." Id., 345, 346.

The borrowing of money by a receiver is certainly discouraged even by those courts which have permitted it. The Supreme Court of the United States, in *Shaw* v. *Railroad Co.*, 100 U. S. 612, say: "For some reason the idea of a receiver and receiver's certificates seems to have been abandoned, and what to our minds was a much more desirable plan, adopted. The power of the courts ought never to be used in enabling railroad mortgagees to protect their securities by borrowing money to complete unfinished roads, except under extraordinary circumstances. It is always better to do what was done here whenever it can be; that is to say, reorganize the enterprise on the basis of existing mortgages as stock, or something which is equivalent, and by a new mortgage, with a lien superior to the old, raise the money which is required without asking the courts to engage in the business of railroad building. The result, so far as incumbering the mortgage security is concerned, is the same substantially in both cases, while the reorganization places the whole enterprise in the hands of those immediately interested in its successful prosecution."

If a receiver has by direction of the court taken moneys and used them, which should not have been so taken, since they belonged to other parties, the court will, for the rectification of the error, order the amount to be returned with interest, to the parties entitled to it: *Meyer* v. *Johnston*, 53 Ala. 347.

While a receiver may borrow money, authority to do so for the purpose of completing a branch, does not warrant a receiver in contracting for municipal aid to enable him to build such a branch: *Smith* v. *McCullough*, 3 Am. & E. R. R. Cases 159.

Where the net earnings of a railroad company are sufficient to purchase rolling stock and equipment, they should be so applied, and receivers will not be authorized to create a loan secured by a car trust for their purchase, merely in order to allow the earnings to be applied to the payment of interest due the bondholders: *Taylor* v. *P. & R. Railroad Co.*, 9 Fed. Rep. 1; 3 Am. & Eng. R. R. Cases 177.

Statutory receivers are strictly limited by the authority conferred upon them by the statute; thus in *Tennessee* v. *E. & K. Railroad Co.*, 6 B. J. Lea 353, a statute of the state provided that in case of the failure of the companies to pay certain bonded indebtedness, the governor should appoint a receiver of the road. Upon the happening of the contingency, he did appoint a receiver, and the question was as to his power to bind the state to pay an indebtedness for materials, &c., created by him as receiver. It was also sought to have these debts declared a first lien upon the proceeds of the sale of the road.

As to the position that the receiver, being an agent of the state, his contract

was the contract of the state, it was decided that this position, if true, would only make the petitioners creditors of the state, and would give them no rights whatever as against the property of the railroad company, nor any lien upon the property of the state, but only a claim against the state, not enforceable by action on account of the state's exemption from suit. It was also decided that the statute authorizing the appointment of the receiver, did not authorize him to contract debts to be paid otherwise than out of the earnings of the road, and further, that there was no obligation on the state to continue the receivership until the current indebtedness of the receivership was paid. The fact that the indebtedness created by the receiver, enhanced the value of the railway property, was decided not to add any strength to the claim, and the petitioners were held not entitled to the relief sought.

An application by receivers to issue certificates to cover certain expenses, and an order of court thereon, accordingly does not bind the receivers or the trust fund to pay particular items of such expenses, the propriety of whose payment is not before the court. And if it appears that certain creditors might at any time have retaken the property for which they ask payment in certificates, and further, that such payment would be to the disadvantage of the trust fund, the court will not compel the receivers to make such payment in certificates: *Coe* v. *N. J. Mid. Railroad Co.*, 27 N. J. Eq. 37.

If prior mortgagees do not assent to receivers' liens, these should be made expressly subject to the prior mortgages: *In re U. S. Roll. St. Co.*, 55 How. Pr. 286.

NATURE AND NEGOTIABILITY.—Receivers' certificates are not debts of the company, but of the receivers, backed by the pledged faith of the court that the property on the proceeds of which they are charged is in its possession, subject to be, and that it will be disposed of by it for the payment of them: *Meyer* v. *Johnston*, 53 Ala. 349. If the fund or property in the hands of the court be not sufficient to pay the certificates in full, then holders of them are entitled only to a *pro rata* share of such proceeds: *Turner* v. *P. & S. Railroad Co.*, 95 Ill. 134.

Generally such certificates contain no express promise to pay, but merely the receiver's acknowledgment of indebtedness. The fund against which they are drawn is uncertain. There is no one personally liable for their payment, which can only be coerced by application to the court which issued them. Only the fund or property under control of such court is bound for their payment, and that only when it is equitable to charge such fund with their payment. While, therefore, it may be within the power of the court to authorize the issuance and sale by the receiver of negotiable paper, yet ordinarily receivers' certificates are not negotiable: *Turner* v. *P. & S. Railroad Co.*, 95 Ill. 134; *Union Trust Co.* v. *C. & L. H. Railroad Co.*, 7 Fed. Rep. 513; *Staunton* v. *A. & C. Railroad Co.*, 2 Woods 506; *Bank of Montreal* v. *C. & C. Railroad Co.*, 48 Ia. 518; *Newbold* v. *P. & S. Railroad Co.*, 5 Bradw. 367.

Nor can the receiver appoint an agent to negotiate them for him. Their issuance and sale is a trust personal to the receiver, and he cannot delegate it to another, and relieve himself of responsibility: *Union Trust Co.*, v. *C. & L. H. Railroad Co.*, 7 Fed. Rep. 513.

If a court orders a receiver to issue certificates of indebtedness, for a specific purpose, to be made payable to the persons to whom it is delivered, or order, and one is issued to A., or bearer, which is negotiated by mere delivery, the holder will take the same subject to all equitable defences against the payee, and the printed order of the court on the back is notice to him that it was made payable to bearer, contrary to the order of the

court authorizing its issue: *Turner* v. *P. & S. Railroad Co.*, 95 Ill. 134.

So, a certificate issued by a receiver to pay debts and expenses incurred by his predecessor, but which is not in fact used on account of any indebtedness made by the former receiver, and for which the receiver issuing it received no benefit, will not be paid at the suit of the payee, or even of a holder for value: *Turner* v. *P. & S. Railroad Co.*, 95 Ill. 134; see also *Union Trust Co.* v. *C. & L. H. Railroad Co.*, 7 Fed. Rep. 513.

In *Humphreys* v. *Allen*, 101 Ill. 490, the court below had authorized the issue and sale of receivers' certificates to pay for indebtedness of the company incurred before the receiver was appointed, and with full notice of a prior mortgage. The Supreme Court express no opinion as to the power of the court to authorize the issuance of certificates for such purpose, but hold that if the holder of railroad bonds secured by trust deeds on the road, having notice of the appointment of a receiver, and an order of court directing him on his petition to issue certificates of indebtedness on which to raise money to discharge a chattel mortgage on the personal property of the company, and to pay taxes, current expenses, &c., and making such certificates a prior and first lien on all the property of the company, desires to question the power of the court to make such order, he must do so before such certificates are issued and sold to *bona fide* purchasers, or paid out to creditors of the company. After their issue and sale it will be too late for him, or purchasers from him with notice of the facts, to raise the question whether the subject-matter to which the certificates were applied, was within the scope of the power of the court in the preservation of the property for the benefit of all concerned. See also *Langdon* v. *V. & C. Railroad Co.*, 53 Vt. 228.

Especially will bondholders be bound when they constitute a committee of their number to represent them in matters appertaining to the management of the property, and such committee consents to the issuance of receivers' certificates: *Langdon* v. *V. & C. Railroad Co.*, 53 Vt. 228. But see dissenting opinion by WALKER, J., in *Humphreys* v. *Allen*, 101 Ill. 490.

INTEREST.—Provision may be made in such certificates for the payment of interest; but the court cannot authorize the receiver to pay usurious rates of interest either directly, as by making them draw a greater than the legal rate of interest, or indirectly, as by fixing their rate of interest at the highest legal rate, and authorizing their sale at a discount. *Meyer* v. *Johnston*, 53 Ala. 352.

PRACTICE.—If the order authorizing the issue of certificates is made without proper notice to all concerned, or is otherwise irregular, the proper mode of objecting to it is by application to the chancellor to vacate and set it aside. *Meyer* v. *Johnston*, 53 Ala. 350.

PAYMENT.—The usual mode of compelling payment of receivers' certificates is by application to the court authorizing their issue. But suppose the property in charge of the receiver has been sold and the court has made a final decree without providing for the payment of outstanding certificates. If the receiver has been discharged, he cannot be sued. The court no longer has either the suit or the property in its control, and is powerless to compel payment of its obligations. Perhaps a purchaser would take the property subject to all claims against the receiver, which might therefore be enforced against him. This was so decided in *Farmers' L. & T. Co.* v. *Central Railroad of Iowa*, 7 Fed. Rep. 537. But in that case the court had especially reserved jurisdiction upon final deree to enforce as liens upon the property all liabilities incurred by the receiver.

REQUEST THAT TRUSTEE FORECLOSE. —The whole debt may be made to become due upon any default in the payment of interest or of principal. *Mallory* v. *W. S. H. Railroad Co.*, 35 N. Y. Superior Ct. 174. The writer has been able to find but one case especially construing the request to the trustee to foreclose. In *Railroad Company* v. *Fosdick*, 106 United States 47, it is held that the clause must be read in connection with the clause in the same article relating to the declaration of default. "The whole article must be taken together." It is to be construed *stricti juris*, with a leaning, if need be, in favor of the debtor, since the declaration of default is in the nature of a penalty or forfeiture.

It was further decided that the written request to the trustees to foreclose was a necessary condition precedent to the foreclosure proceedings; that it was not optional with the trustees to foreclose without such request, but that the latter was intended to secure to a majority of the bondholders "the right to veto the proceeding of the trustees." "Many cases may be mentioned," say the court, "to illustrate the importance in their interests of such a control, rather than to put it in the power of one, or a minority, to require all to accept what the majority might consider to be premature and less valuable satisfaction for their existing security. The larger number might think it to their advantage even to defer the collection of their overdue interest, much less not to anticipate the payment of the principal, even when the security was ample to meet both; for they might esteem the ultimate investment higher than present payment. While they could not and ought not to prevent others, even a single individual, from exacting the promptest payment of what is due and may be important as current income, by legal process, they may nevertheless rightfully object to an anticipation of payment that may in their opinion prove to be a sacrifice. And this becomes especially important when the present value of the security is insufficient to prepay the incumbrance, but contains the solid promise of future indemnity as an investment."

Chief Justice WAITE and Justice HARLAN dissented, holding that if no request were made, the trustees were not precluded from commencing foreclosure proceedings on their own motion. *Railroad Co.* v. *Fosdick*, *supra*.

It has also been decided that a trustee will be left to exercise his discretion as to the time of making sale under a decree of foreclosure, and as to making sale at all pending an appeal from the decree which the appeal does not supersede. *Farmers' Loan & Trust Co.* v. *Central Railroad Co. of Iowa*, 4 Dill. 546. And this, notwithstanding a committee of the bondholders requested the trustee to order a special master to proceed with the sale, and tried to compel him to accede to their request by application to the court.

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